

ETA Conjoint Research

OMB #1510-0071

FINAL REPORT AND MARKET MODEL
UNBANKED FEDERAL CHECK RECIPIENTS

Prepared by Dove Associates, Inc.

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Preface

About Dove Associates

Dove Associates, Inc. has been advising clients in the Financial Services industry since the early 1980s. We have performed projects for a variety of financial institutions, processors, associations, and EFT networks, primarily focused on strategic business analyses combined with research and development of product and market strategies.

Our Financial Services Group works in all areas of card payment products (ATM and Debit, Credit Cards and Smart Cards, and EBT), Online Banking, Electronic Bill Payment and Presentment, E-Commerce, Operational Excellence, and Bank Distribution Strategy.

Dove Associates has conducted numerous conjoint studies for financial institutions and consumer products firms that are seeking to develop new products and need to understand customer preferences.

Examples of some of our recent work include:

- Published the “1999 Debit Card Study”.
- Published the “1997 Payment Preferences Study”.
- Published “The Future Use of ATMs,” an industry white paper assessing the state of the ATM industry and evaluating threats to ATM volume going forward.
- Developed the business case for EFT network consolidation for a leading association of financial institutions.
- Formulated ATM growth strategies for leading ATM deployers.
- Developed PC banking market-entry strategies.
- Redesigned the back office operations of a major ATM deployer to improve efficiency and decrease cost.

In addition to our Financial Services Group, Dove has other practices focusing on Beverage & Food, Consumer Broadband, Accelerated Business Transformation, and Performance Improvement.

Dove has offices in Boston, Atlanta, Charlotte, Minneapolis, San Francisco, and London.

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Executive Summary

1.1. Introduction

Objective

Dove Associates conducted a research study on behalf of Treasury/FMS to estimate the demand for various low-cost bank account configurations for Federal check recipients who do not have a depository account at a financial institution.

Methodology — Overview¹

A paper-based questionnaire was developed as the primary research instrument to understand opinions concerning bank accounts from the perspective of Federal check recipients who do not have an account at a financial institution.

A variety of hypothetical product configurations that centered around proposed elements of the Electronic Transfer Account (ETA) were tested using choice-based conjoint (CBC) analysis. This methodology provided a way to understand preferences and predict choices that unbanked Federal check recipients would make regarding various combinations of features available.

In the conjoint section of the survey, respondents were given a series of hypothetical ETA products and asked to select which, if any, they would voluntarily choose.

¹ This survey achieved a 61% participation rate. According to the terms of clearance by the Office of Management and Budget, since the survey did not achieve a response rate of at least 70%, and follow-up attempts to survey non-responders did not generate the required 80% participation rate, it cannot be considered representative of the population.

The conjoint survey tested the following features:

ETA Features Tested in Conjoint Analysis

Feature	Feature Options			
Deposits Accepted	Federal only	Federal and other		
Interest on Balances	None	2%		
Bill Payment	Same as today	Automatic or same as today		
Access Points	ATM only	Store cashier or ATM	Bank teller or ATM	Bank teller, store cashier, or ATM
Monthly Cash Withdrawals	3 free	4 free	5 free	
Monthly Fee	\$2.00	\$3.00	\$4.00	

Table 1.1

In addition, the survey also gathered data about respondents' attitudes, access to financial services, and demographic characteristics. This information provides a means of assessing the validity of the CBC results. The reader is cautioned to take care in interpreting the demographic segmentation data presented in this report due to the limited sample size.

Methodology — Sample Base

The sample base and the conjoint questionnaire were designed with a goal of achieving national representativeness for the survey, with respect to consumer preferences about potential ETA features. Based on the binomial distribution of the conjoint methodology, it was determined that a sample of 384 unbanked recipients could provide results within five percent at a 95% confidence level.

Although the conjoint study of potential ETA features can achieve national representativeness with 384 respondents, with this sample size the demographic and attitudinal data provided as background do not meet the sample size requirements for national representativeness established by the Office of Management and Budget (OMB).

For this conjoint study, all respondents received a written survey in the mail. Unbanked check respondents were from two sources:

- One group of check recipients was pre-screened on the telephone to identify recipients who did not have a bank account and who were willing to complete the conjoint survey. After telephone screening they received a written survey in the mail.

- In order to reach a sample of unbanked check recipients who may not have phones, a second group of check recipients, with no telephone number available, including both banked and unbanked recipients, received a mail survey directly.

The written survey responses were separated into those with a bank account and those without a bank account. The pool of unbanked respondents therefore includes some individuals who were phone screened and some who received the survey directly.

The sample database provided by FMS was matched with publicly listed telephone numbers. As a result, 41% of the names were matched, of which 2,000 were randomly selected. A telephone screening of these 2,000 Federal check recipients was conducted to identify recipients without a bank account. With a maximum of three attempts to contact each recipient, 211 unbanked Federal check recipients had volunteered to participate. For recipients who did not match up with a telephone number, screening was not possible and a survey mailing was necessary to ensure an equal chance of participating and to avoid systematic bias. Therefore, questionnaires were mailed to 2,000 randomly selected recipients with no phone number. Of the 2,211 total surveys initially sent out, for reasons including bad address, death and direct deposit conversion, 222 surveys were classified as invalid and the sample base was revised down to 1,989 unbanked recipients. The 222 invalid surveys number might be due to the fact that the sample run of check recipients was obtained by FMS from July 1998 databases and the survey was conducted in the first quarter of 1999.

The scope of the research was national. Surveys were sent to all 50 states, the District of Columbia, and Puerto Rico, in proportion to the overall Federal check recipient geographic distribution. The study was also conducted across multiple Federal benefit programs including Social Security Administration, Supplemental Security Income, Veterans Affairs, Office of Personnel Management, and Railroad Retirement Board.

Methodology — Response Rate

A total of 846 completed surveys were returned and included in the analysis. Out of this total, 385 respondents did not have a bank account and 461 had a bank account, yielding an overall response rate of 43%. However, for the targeted population of unbanked Federal check recipients, the response rate is 61%. This is based on the assumption from prior Treasury/FMS commissioned research by Shugoll Research/Booz, Allen & Hamilton that 27%² of the Federal check recipients without a phone number who were sent a survey were unbanked.

² The assumption of a 27% unbanked rate for a mail survey was based on a Treasury/FMS commissioned study conducted by Shugoll Research. This result was based on sampling data and therefore subject to variability. This study was based on a survey with a response rate of 42%, which meant, according to Shugoll, that their results were reliable to plus or minus 3.6 percentage points at the 95% confidence level.

Unbanked Response Rate

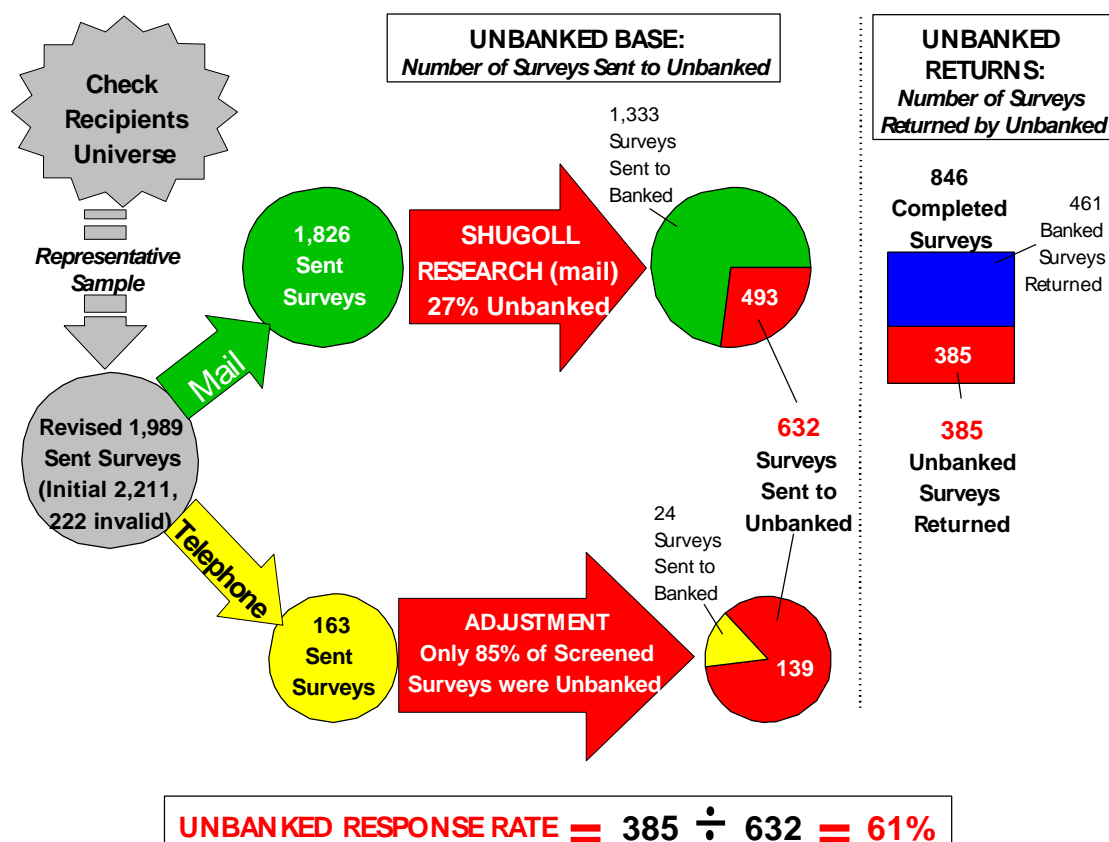


Figure 1.1

A 61% response rate is substantially higher than private sector standards³ for national projectionability, but does not meet OMB's 70% response rate standard requirement. Therefore, the results presented in this report cannot be, applying OMB standards, projected nationally to the overall unbanked Federal check recipient population.

Survey Participants Profiles

Of 385 unbanked Federal check recipients who participated in the study:

- 58% were female; 42% were male.
- 42% lived in cities, 8% in suburbs, 27% in small towns, and 23% in the countryside.
- 52% were White, 25% Black⁴, 14% Hispanic⁴, and 9% Other ethnic group.
- 30% had an annual household income under \$6,000, 54% between \$6,000 and \$15,000, and 16% over \$15,000.

³ Church, "Incentives in Mail Surveys: A Meta Analysis", Public Opinion Quarterly (1993), 57, 62-79.

⁴ Which is higher than the percentage of Blacks and Hispanics in national census statistics, or among banked recipients.

1.2. Key Observations⁵

Twelve key observations from the research and analysis are presented below by category:

Unbanked Federal Check Recipients Check Cashing Practices

1. Most unbanked Federal check recipients are satisfied with the way they cash their checks.

Seventy-one percent of unbanked are satisfied with the way they currently cash their Federal checks. Sixty-nine percent of unbanked respondents think that it is easy to cash their Federal checks. In addition, 70% think that the location where they cash their Federal checks is convenient.

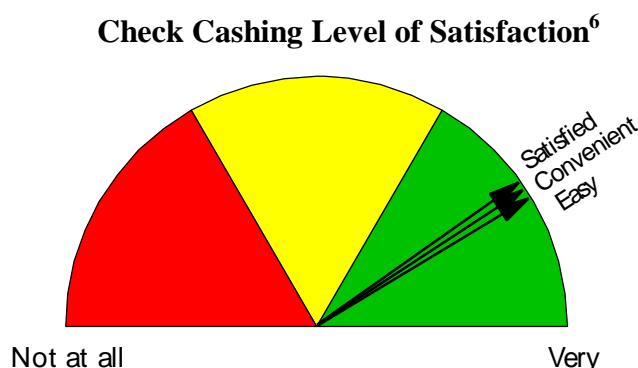


Figure 1.2

2. One factor contributing to the high degree of satisfaction among unbanked recipients is that a minority (39%) is charged a fee to cash their Federal checks.

In general, check cashing is inexpensive because 51% of unbanked Federal check recipients go to financial institutions (banks or credit unions) where they can usually cash their checks at no charge: specifically, 81% of unbanked recipients who go to financial institutions do not pay a fee to cash their checks.

Unbanked Federal Check Recipients' ETA Preferences

3. Logically, unbanked recipients who now pay a fee for check cashing are significantly more interested in an ETA that would charge a monthly fee.

Conversely, unbanked recipients who cash their checks for free are less interested in an ETA. Specifically, 46% of the unbanked Federal check recipients report no interest in an ETA regardless of the features proposed at any of the three monthly fee levels tested (\$2.00, \$3.00 and \$4.00).

4. For the 54% of unbanked recipients interested in some form of an ETA, the most important decision factor is access (how often and where they can get cash), followed by the cost of the ETA, and to a lesser extent by optional features (interest paid, deposits allowed, and electronic bill payments).

⁵ The sample data contained in this section is subject to variability and are not point estimates alone. Additional information is contained in the Methodology section, Chapter 3.

⁶ All charts of this type are based on 13 point scales.

Relative Importance of ETA Features Unbanked Respondents Interested in ETA

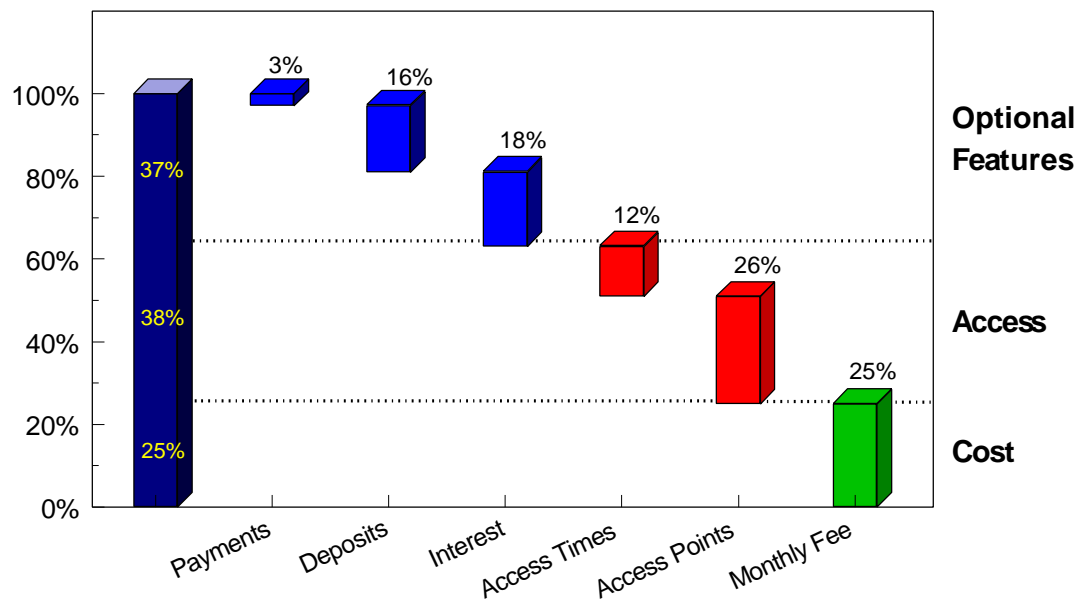


Figure 1.3

- Within each of these features, respondents' preferences were identified. The preferences were then incorporated in the modeling to estimate demand for various ETA configurations. The results of the conjoint appear to be rational, in that respondents consistently prefer the option with the greatest value (the richest option at the lowest cost).

ETA Feature Preferences

	<div> <div>Most Preferred</div> <div></div> <div>Least Preferred</div> </div>		
DEPOSITS ACCEPTED	Federal and Other		
INTEREST ON BALANCES	2%		
BILL PAYMENT	Automatic or same as today		
ACCESS POINTS	Bank teller, store cashier or ATM	Store cashier or ATM	Bank teller or ATM
MONTHLY CASH WITHDRAWALS	5 free	4 free	3 free
MONTHLY FEE	\$2.00	\$3.00	\$4.00

Figure 1.4

- Using conjoint methodology, trade-offs between features — with their respective preferences — can be measured and modeled to predict demand for specific product configurations. Five product configurations were analyzed in detail. The five configurations and their respective demand or 'take-rate' are presented below in Figure 1.5.

**‘Take-Rate’ for ETA Configurations
at a \$3.00 Monthly Fee
with 4 Free ATM Cash Withdrawals**

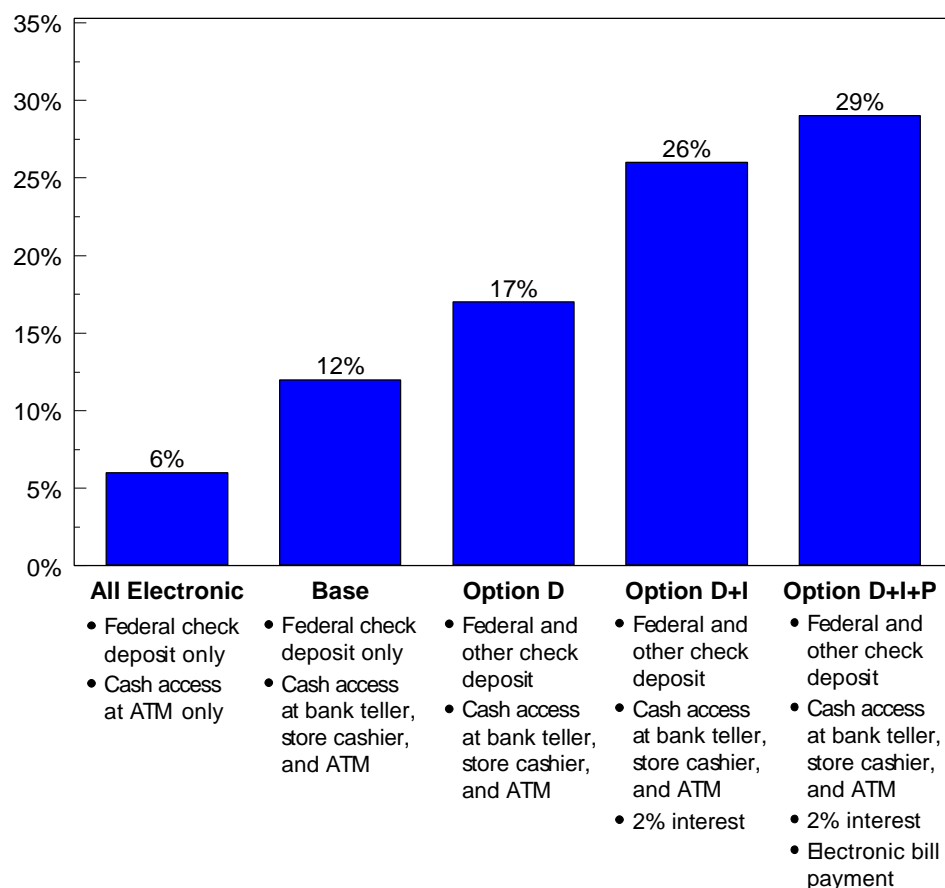


Figure 1.5

Of those five configurations, an ‘all-electronic’ ETA configuration is the least preferred. This product, at a \$3.00 monthly fee level, would be chosen by approximately 6% of the current unbanked Federal check recipients.

The other four configurations each progressively incorporate more access and the proposed optional features. These product enhancements could increase the number of unbanked recipients who would choose an ETA by nearly five-fold (from 6% to 29%). This increase is driven by:

- Access to bank tellers and store cashiers
- Payment of 2% interest on account balances
- Acceptance of deposits from other sources than Federal only

7. The five configurations were tested at three different price levels (\$2.00, \$3.00, and \$4.00 per month). The resulting ‘take-rates’ reflect respondent choices when presented with the binary choice of enrolling in the ETA as described or remaining without an account. Because respondents were offered product choices at \$2.00 per month, the estimated enrollment at \$3.00 per month may be conservative. Some survey respondents will always prefer the least expensive product, but will actually sign up at the higher price when the product is not available less expensively. Holding all of the other features constant, price sensitivity and elasticity analyses suggest that a \$3.00 monthly fee may be acceptable to recipients.

**‘Take-Rate’ for ETA Configurations
by Monthly Fee**

ETA Configuration	\$4.00	\$3.00	\$2.00
All Electronic	4%	6%	9%
Base	9%	12%	18%
Option D	14%	17%	26%
Option D+I	21%	26%	37%
Option D+I+P	24%	29%	41%

Table 1.2

As expected, the \$2.00 monthly fee option was the most popular among unbanked recipients, as it was the lowest price available to respondents. Since 61% of recipients currently cash their checks for free, a \$2.00 fee might not be the optimal price level.

Unbanked Federal Check Recipients’ ETA Preferences by Segment

8. In addition, respondents’ interest in the ETA varies strongly by demographic segments. The most interested segments are unbanked recipients living in cities, Black unbanked recipients, and unbanked recipients under 35 years old.

As shown in Table 1.2, at a \$3.00 monthly fee, the ‘take-rate’ for the overall unbanked population would range from 6% for an ‘all electronic’ ETA to 29% for ‘Option D+I+P’. Specifically, for unbanked recipients living in cities, the ‘take-rate’ would range from 8% to 34%. For Black unbanked recipients, the ‘take-rate’ would range from 9% to 48%. For unbanked recipients under 35 years of age, the ‘take-rate’ would range from 6% to 49%.

9. City unbanked Federal check recipients are more likely to choose an ETA than unbanked recipients living in other areas outside of cities.

As shown in Figure 1.6, for all ETA configurations, the ‘take-rate’ of city unbanked recipients is at least 54% greater than that of countryside unbanked recipients and at least 42% greater than that of small town unbanked recipients.

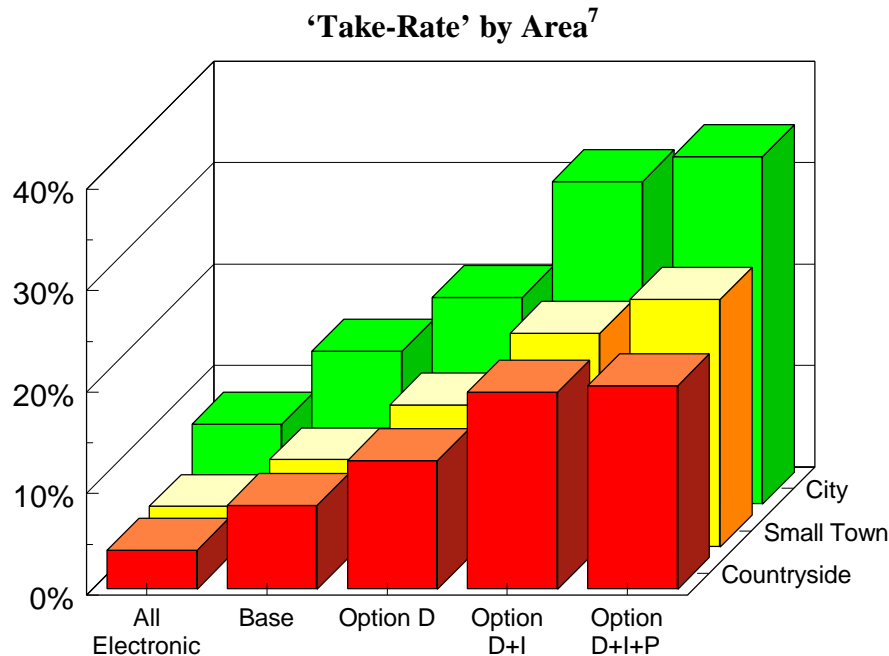


Figure 1.6

This is consistent with the previous result showing that unbanked recipients who now pay a fee for check cashing are significantly more likely to be interested in an ETA which would charge a monthly fee. Unbanked Federal check recipients living in cities are more likely (53%) to be charged check cashing fees than recipients in the countryside (26%) or small towns (29%).

10. Black unbanked Federal check recipients are more likely to choose an ETA than other groups.

As shown in Figure 1.7, for all ETA configurations, the ‘take-rate’ of Black unbanked recipients is at least 63% greater than that of White unbanked recipients and at least 80% greater than that of Hispanic unbanked recipients.

⁷ Suburban segment not included due to small number of responses for that segment.

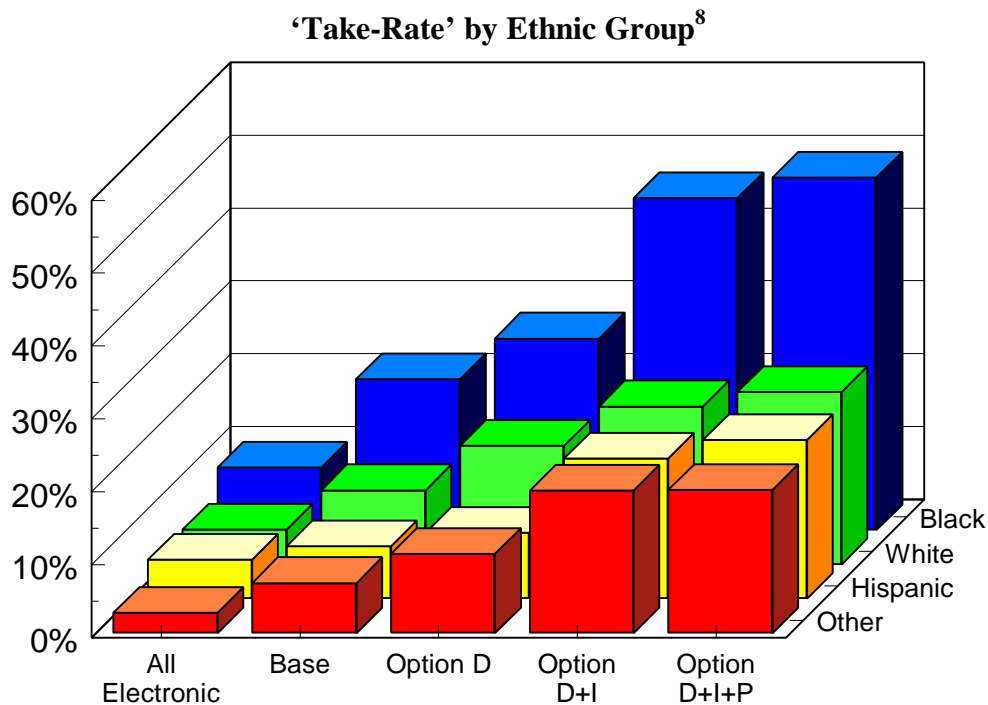


Figure 1.7

Black unbanked recipients show greater receptivity to ETAs because 62% are charged a fee to cash their checks compared to Whites (27%) or Hispanics (40%). This is associated with key observation #2, in that Black unbanked recipients are less likely (34%) to use financial institutions than Whites (62%) and more likely (33%) to use check cashers than Whites (7%).

11. Unbanked respondents under the age of 35 are more interested in the ETA than other age groups, suggesting that ETA acceptance should grow over time.

As shown in Figure 1.8, the ‘take-rate’ of unbanked recipients under 35 years of age for ETA ‘Option D+I+P’ is 345% greater than the interest of unbanked recipients over 74 years of age.

⁸ Other includes Asian, American Indian or Alaska Native, Native Hawaiian or Pacific Islander.

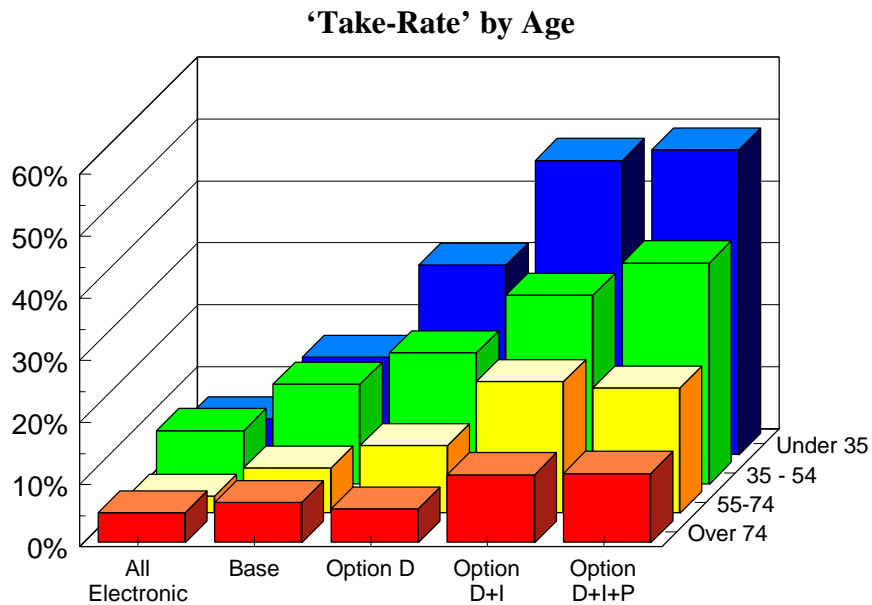


Figure 1.8

Potential ETA Customers Among Unbanked Federal Check Recipients

12. A Market Model was designed based on the conjoint analysis. The model incorporates all the variables including features and segmentation, and multiplies the resulting ‘take-rate’ by the estimated number of unbanked Federal check recipients, in order to assess potential demand for the ETA. The Market Model predicts that approximately 276 thousand to 2 million unbanked Federal check recipients would voluntarily choose an ETA, depending on the features offered.

For the five ETA account configurations, ‘All Electronic’, ‘Base’, ‘Option D’, ‘Option D+I’, and ‘Option D+I+P’, the table below displays the ETA demand that would be expected at a \$3.00 monthly fee level.

‘Take-Rate’ and Expected Number of ETA Accounts at a \$3.00 Monthly Fee

Option (\$3.00)	‘Take-Rate’	Low Case* Number of ETA Accounts (000)	High Case** Number of ETA Accounts (000)
All Electronic	6%	276	386
Base	12%	585	818
Option D	17%	855	1,197
Option D+I	26%	1,302	1,822
Option D+I+P	29%	1,433	2,007

Table 1.3

*Low case assumes 5MM unbanked Federal check recipients.⁹

** High case assumes 7MM unbanked Federal check recipients.⁹

⁹FMS/Treasury commissioned report, ETA Initiative Final Report, Dove Associates, June 15, 1998 — “ ETA prospects who do not have a bank account at an FI represent 24% of the Federal benefit check recipient population (based on Shugoll Research) — approximately 5.2 to 6.5 million individuals”.

The Market Model may provide useful information for financial institutions to consider offering and marketing an ETA product in their local market. Based on the conjoint survey, the Market Model provides estimated ‘take-rates’ for various ETA configurations for consideration by a financial institution. The results carry the same degree of accuracy and national representativeness as the conjoint study itself. Please refer to the Methodology section for more detail.

Key Findings

1. Over time, two primary factors will drive greater acceptance of ETA offerings. First, greater interest in the ETA among young unbanked recipients may translate into higher demand for the ETA as the unbanked recipient population ages. Second, the current trend of banks and retailers increasingly charging for check cashing may stimulate further demand for ETAs.
2. Across the five configurations examined, the ETA will be more readily adopted by unbanked check recipients who live in cities, who are Black, or who are under 35 years of age. The Federal government should give top priority to these three segments in order to achieve the greatest sign-up for the ETA and to support financial institutions’ marketing programs. Financial institutions and Treasury will find that these segments will be the easiest to convert from paper checks to electronic payments.
3. Different ETA configurations receive different levels of demand because not all features are equally attractive. Access is a critical dimension. The Federal government should consider the importance of cash access in locations that can offer personal attention such as bank tellers or grocery store clerks, as opposed to all electronic access. First, this provides a wider range of cash access locations (financial institutions branches, stores) and assistance for unbanked recipients. Second, this also gives financial institutions a cross-selling opportunity to draw unbanked recipients into the banking mainstream. In addition, respondents’ answers indicate that financial institutions that pay interest on the account and permit additional deposits will make the ETA more attractive.
4. As a result, to maximize the demand for an ETA, we recommend that the Federal government consider adopting the Option D+I at a \$3.00 monthly fee. This option provides the best balance between financial institution supply and unbanked recipient demand — pricing must be balanced between what FIs are able to provide and what unbanked are willing to pay. If financial institutions cannot cover their costs from ETA accounts, they will not be likely to offer ETAs on a voluntary basis.

Background

2.1. Situation

The Debt Collection Improvement Act requires Treasury to issue all payments (except tax refunds) beginning January 1, 1999, by electronic transfer. This change will greatly affect paper check recipients who will be encouraged to participate in the Direct Deposit program. The law presents an even greater challenge to check recipients who do not have a bank account. Treasury is assisting recipients who can conveniently establish an account by helping them to enroll in the direct deposit program. However, the law also requires Treasury to make a low-cost account available for those who are not able to establish a bank account for various reasons, including the prohibitive price of commercially available accounts.

According to earlier demographic studies, FMS estimated that there are approximately five to seven million Federal check recipients who may need an ETA. The conjoint research study examined the preferences and sensitivities of these prospective customers around various potential low-cost bank ETA account configurations. Dove Associates was engaged by FMS as a subcontractor to PricewaterhouseCoopers to conduct market research using conjoint analysis for Electronic Transfer Account (ETA) product positioning and optimum client use.

The research project began in October 1998 and was completed in May 1999. The survey was administered during the months of February and March 1999.

2.2. Research Objectives

This research focused on potential ETA customers who are Federal check recipients and do not have a banking relationship. Conjoint Analysis was needed to estimate potential customers' preferences for various features and pricing of the ETA in order for them to receive Federal benefit payments electronically.

The study was designed to test different hypothetical features and fees of specially designed bank accounts for potential ETA customers, and to produce a market model to predict the acceptance of the ETA by various customer segments. The research will be used to project customers' future choices about hypothetical ETA features and associated fees.

Conjoint analysis is a research technique that has been used for more than twenty years to measure the value that respondents derive from various product features. It is a technique that decomposes products and/or services into discrete components and then methodically varies the product configurations and measures consumers' responses to the changes.

In a typical study, respondents are asked to rate their interest in purchasing a range of possible product bundles referred to as conjoint profiles. Each profile includes different levels (e.g., prices, features, etc.) for selected features that make up the product or service. By methodically repeating this process, it is possible to quantify those features that a respondent likes and dislikes, and to determine the strength of that preference.

In order to gain an understanding of the likely response to various ETA configurations, Dove used a Choice-Based Conjoint methodology which permitted respondents to indicate their preferences in a multiple-choice format that included a 'no sale' option (i.e., "Which, if any, of these products would you select?"). The share of choice is used to assess 'take-rates' for each configuration.

Given the economic and educational profile of the unbanked, it was determined that the survey should be paper-based and that the number of product features should be limited to six in order to minimize respondent fatigue.

This research provides a quantitative basis for strategic product decisions around ETA features and pricing and will permit Treasury/FMS to model the impact of various fees and features, for maximizing conversion of the entire market. The features tested included:

- Monthly fees
- Monthly cash withdrawals
- Cash access points
- Automatic bill payment
- Interest paid on balances
- Deposits from Federal and other sources

In addition to the conjoint research, attitudinal, behavioral and demographic data was collected in the survey to permit a better understanding of why respondents made the product choices they did in the conjoint section of the survey.

The challenge of this study is to provide demand-side information which can be used by Treasury to estimate the market equilibrium point where demand for ETAs by unbanked Federal check recipients and supply of ETAs from FIs meet.